

Message Text

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TO AMEMBASSY JAKARTA

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TAGS: ENRG, EFIN, ID, US

SUBJECT: USG-GOI TAXATION OF U.S. OIL COMPANIES

1. WILLIAM J. CASEY, FORMERLY EXIM BANK PRESIDENT AND NOW WITH ROGERS AND WELLS, CALLED ON INDONESIAN ECONOMIC COUNSELOR ADIWOSO AUG 30 TO BRIEF HIM IN GENERAL TERMS ON RECOMMENDATIONS LAW FIRM WILL BE PRESENTING TO GOI. CASEY THINKS HE WILL BE READY TO CABLE "WHOLE PACKAGE" TO SADLI VERY SHORTLY. PACKAGE WILL INCLUDE TEXT OF A NEW MODEL CONTRACT FOR USE WITH PRODUCTION SHARING COMPANIES AND SOME IDEAS FOR NEW TAX LEGISLATION, INCLUDING TEXT IF DESIRED. CASEY HAS CONSULTED WITH IRS OFFICIALS AND ACCEPTS THEIR POSITION THAT THEY CANNOT COMMENT AUTHORITATIVELY AT THIS TIME ON THE U.S. TAX EFFECTS OF ONLY A MODEL CONTRACT AND SOME HYPOTHETICAL TAX LEGISLATION. IF GOI APPROVES ROGERS AND WELLS PROPOSALS, HOWEVER, IT MIGHT AUTHORIZE R AND W TO WORK WITH ONE OIL COMPANY TO PREPARE A SINGLE "TEST APPLICATION" FOR AN IRS RULING, OR ELSE GOI MIGHT SIMPLY ADVISE ALL OIL COMPANIES OF NATURE OF PROPOSED NEW CONTRACT AND TAX LAW AND LET EACH COMPANY DECIDE FOR ITSELF WHETHER AND HOW

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IT WISHES TO APPROACH THE IRS. CASEY SAID HE WOULD BE

"FACTORING IN" PROPOSED NEW U.S. TAX PROVISIONS ON U.S. TAX CREDITABILITY OF FOREIGN TAX PAYMENTS (SEE PARA 3 BELOW).

2. LAWYER FOR NATOMAS (NORDBERG) REPORTS THAT SENATE-HOUSE CONFEREES HAVE REDUCED EXTENSION OF TAX SITUATION EXISTING PRIOR TO IRS RULING, WHICH PROVIDES SOME RELIEF FOR PRODUCTION-SHARING COMPANIES, FROM FIVE YEARS TO ONE YEAR. NORDBERG STILL NOT CLEAR WHETHER "ADDITIONAL ARRANGEMENTS" AGREED TO BY HIS CLIENT IN EARLY AUGUST WITH PERTAMINA WOULD REMOVE NATOMAS' PROTECTION FROM IRS 76-215 RULING UNDER GRANDFATHER CLAUSE. NORDBERG SAID NATOMAS WOULD BE APPLYING FOR AN IRS RULING SOON.

3. PRESS REPORTS THAT SENATE-HOUSE CONFEREES AGREED AUG 31 ON PROVISION IN TAX BILL PROVIDING THAT CREDIT WHICH U.S. OIL COMPANIES CAN TAKE FROM THEIR FOREIGN INCOME TAXES AND APPLY TO THEIR U.S. INCOME TAXES SHALL BE LIMITED TO 48 PERCENT OF FOREIGN TAXABLE INCOME. FORMERLY, LIMIT HAD BEEN 50 PERCENT. WE UNDERSTAND THAT THIS NEW PROVISION DOES NOT ADDRESS QUESTION OF WHAT IS A CREDITABLE TAX BUT SIMPLY ASSUMES THAT PAYMENTS U.S. OIL COMPANIES MAKE TO HOST GOVERNMENTS ABROAD ARE TAXES WHICH WOULD BE CREDITABLE IN WHOLE OR IN PART AGAINST U.S. TAXES. BY THE TERMS OF IRS' JULY 14 NEWS RELEASE (STATE 177348), HOWEVER, IT IS CONCEIVABLE THAT MUCH IF NOT MOST OF SUCH OIL COMPANY PAYMENTS WILL HAVE TO BE REGARDED BY IRS AS ROYALTIES AND NOT TAXES.

4. IT IS OUR UNDERSTANDING THAT IRS PREFERS TO BASE ITS RULINGS ON CONTRACTS WHICH TAXPAYER HAS ACTUALLY SIGNED AND ON FOREIGN TAX LEGISLATION WHICH HAS ACTUALLY COME INTO EFFECT. IRS RULINGS HAVE BEEN GIVEN, HOWEVER, ON BASIS OF SPECIFIC (NOT MODEL) CONTRACTS WHICH TAXPAYER IS FULLY PREPARED TO SIGN. RULING GIVEN ON SUCH BASIS MIGHT OF COURSE LOSE ITS VALIDITY IF CONTRACT WHICH TAXPAYER SUBSEQUENTLY SIGNED WAS AMENDED SIGNIFICANTLY. WE BELIEVE IRS IS VERY HESITANT TO GIVE RULING BASED ON EXAMINATION OF PROPOSED FOREIGN TAX LEGISLATION, BECAUSE SUCH RULING MIGHT LOSE VALIDITY IF ACTUAL LAW PASSED DEVIATED FROM LEGISLATION PROPOSED.

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5. IT OCCURS TO US THAT USG AND GOI MIGHT CONCEIVABLY DIFFER ON THEIR VIEWS OF THE VALUE OF A U.S. OIL COMPANY'S RESERVES OF HYDROCARBONS IN ITS AREA OF OPERATIONS IN INDONESIA, SINCE THE IRS' CONCEPT OF "AN APPROPRIATE ROYALTY OR OTHER CONSIDERATION HINGES ON SUCH VALUATION. KISSINGER

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